Crore talent

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India's project finance business, like its Chinese counterpart, has become an almost exclusively local affair. A local bank debt deal will fund the landmark New Bangalore International Airport project, while Petronet's long-term project loan has also been syndicated entirely to Indian institutions.

The financing for Bangalore International Airport Ltd (BIAL), which will be the owner and operator of the airport, is expected to close this year but certain key issues, including the debt and equity split, and the level of state support, are still under discussion. According to Dr Wolfgang Bischoff, a managing director at Siemens Project Ventures, one of the BIAL investors, the funding is likely to be spilt roughly as follows: 25% equity, 25% state support and a little over 50% debt (the total project cost is estimated at about $270 million). State support is expected in the form of a long-term interest-free loan from the Karnataka state government.

The commercial loan will be a non recourse facility, with ICICI Bank the sole lead and underwriter. Mohit Batra, manager of ICICI's project finance department says the term will be more than 12 years.

In the early stages of planning the financing, Bischoff says the sponsors considered export finance options. "But because Siemens itself has an Indian manufacturing capability and will source some of the equipment through our Indian industrial partner, Larsen and Toubro, more than two thirds of the equipment will be supplied from India. Export finance could therefore only have covered a relatively small amount of the total financing."

Siemens Project Ventures, which acted as the financial adviser, recommended that an export finance element should be rejected to keep the financing structure relatively simple, and to avoid foreign exchange risk. (BIAL's revenues will be entirely in Rupees). "The airport's main revenue base will be passenger and cargo aeronautical fees, and this is what our business plan is based on," says Bischoff. The managing director adds that the proportion of non-aeronautical fees in the income mix is not likely to be as high as some European greenfield airports are able to achieve (where some airports have been able to push retail and other revenues to 50% of the total).

The construction period for the airport is estimated at 33 months, and is due to begin immediately after financial close.

Petronet lures banks

Like BIAL, the Petronet project, India's first operational liquefied natural gas (LNG) importing terminal, is relying on Indian institutions for the long-term project loan. The project's overall financing reached close this year. But the $450 million equivalent long-term non recourse facility was put together in 2003. Prosad Dasgupta, director of finance for Petronet, says that the project loan (with a tenor of 12 years door to door), led by State Bank of India, included a total of 15 Indian banks and development finance institutions. All the state banks were represented in the deal, as well as Infrastructure Development Finance Corporation (IDFC) and ICICI. The loan is denominated in local currency, as proposed by the financial adviser (ABN Amro), partly because of the strong local bank appetite.

The total cost of the project is IRP25.76 billion ($600 million), of which IRP18.04 billion is financed by debt and IRP7.72 billion by equity. In addition to the long-term loan, the project debt package includes approximately IRP 7.5 billion of standby letters of intent in favour of the LNG supplier and the ship owners and IRP2.5 billion of working capital loans, says Dasgupta.

Unusually, the long-term financing has been put in place after the construction of the facility. In fact, the receiving, storage and regasification site in Gujarat commenced operations three months before the March financial close.

Raj Pande, head of Asian project finance for Paul, Hastings, Janofsky & Walker (lawyers to the Petronet investors), says the original sponsors, the Indian state-owned oil and gas majors, Indian Oil Corporation; Gas Authority of India, Oil and Natural Gas Corporation, decided not to have the long-term financing in place until after the EPC contract was awarded. Initial short-term funds were raised backed by the corporate guarantees of the sponsors on the understanding that these interim loans would be fully repaid once the long-term funding was in place.

Petronet's sponsors subsequently included Gaz De France, with a 10% stake, but even after the EPC contractor was appointed, financing proceeded on a short-term, corporate basis. Sponsor guarantees were originally to expire in June 2003, but were extended twice while the long-term financing was being arranged, eventually until 30 June, 2004. Dasgupta says a portion of the long term debt has now been drawn to pay off the original guaranteed loans.

The long-term funding also includes capital raised via an IPO in March. Petronet was able to raise IRP3.91 billion from the issue, led by SBI Capital, Merrill Lynch, Enam Financial Consultants, ICICI Securities and Morgan Stanley.

According to one banker, foreign institutions did not bid aggressively for the Petronet financing largely because of doubts over customer demand for LNG in India.

But the more pessimistic banking assessments appear to have been proved wrong, at least regarding initial demand. Petronet has sold its first 5 million tonnes with ease. According to Dasgupta, only industrial users were able to secure first round supply from Petronet, while fertiliser producers and power companies committed to buy the second 2.5 million tonnes of Petronet's LNG (total current capacity is 5 million tonnes). Another major potential state buyer, the Ministry of Chemicals & Fertilizers, has placed an order for 2.5 million tonnes at current market prices. This amount is in addition to the 5 million tonnes already sold.

However, the real test of market demand has yet to come. "Shell also has an LNG import venture in India which is due to receive its first LNG cargo at the end of the year. We will have a better idea of total market demand once the two projects are competing head to head," says one source. The Shell project was financed on balance sheet.

Undaunted by Shell's entry into the market, Petronet is pressing on its expansion plans. "We aim to add two more tanks in the 36 months to take capacity to 13 million tonnes of LNG per year by 2008," says Dasgupta. The official says that this expansion will cost an estimated IRP10 billion.

"The funding will be roughly 70% debt and 30% equity. But IRP1.55 billion of the equity amount will come from IPO proceeds," says Dasgupta.

The director of finance believes that Petronet could easily raise the entire expansion-related debt from the Indian bank market. We could raise IRP700 million in 7 minutes," he says. "We know the appetite is clearly there, as the Indian banks who are in the long-term project loan only got half of what they subscribed for." Dasgupta believes that bank appetite has been further boosted by Petronet's stronger than expected initial results. The company managed to post a modest profit in its first ever quarter, compared with a projected cash loss of IRP680 million.

Can bonds break in?

However, Petronet may look for a bond issue, rather than more bank debt, to finance the expansion. The company already plans a IRP500 billion bond programme in September or October this year to repay the project finance bank loan. The bond will benefit from a partial guarantee from the Asian Development Bank (ADB) and is expected to be rated AA+. With the ADB support, Dasgupta says the cost of the capital markets debt could be below 7%, compared with 9% for the project loan. This year's bond program will mirror the redemption period of the project finance loans to allow the one to replace the other, says Dasgupta. "There will actually be three separate bond issues, reflecting the repayment profile of the bank loan," he adds.

Dasgupta reveals that his company has also been in discussions with Germany's KfW, to whom the ADB will sell a portion of its exposure.

In the case of the Bangalore airport development, the option of a capital markets financing to replace the long-term project loan has not yet been discussed. "An equity market listing or a bond issue are certainly options," says Bischoff, "but we won't really be in a position to think about these opportunities until the airport is operating. According to the concession agreement, the private investors in BIAL are also contractually bound to remain in the project. "For that reason, it certainly wouldn't be possible to have a full float of BIAL's shares on completion of the airport."

In general, debt capital markets funding is still a rarity for Indian projects. Sunny Singh, in ABN Amro's structured capital markets team in Singapore, says: "the main investor base is the Indian banking sector itself, therefore in view of the sufficient liquidity within the system and the ability of banks to take and hold positions, it doesn't usually make sense to go through the process of getting a rating and issuing a bond." The Petronet bond is an exception because of the ADB's involvement and Petronet's very strong sponsor group.

The Petronet and BIAL project loans underscore that Indian institutions will be the primary bank debt providers for upcoming projects. This is despite the fact that two major loan providers during the 1990s, IDBI and IFCI (Industrial Financial Corporation of India), have curtailed their lending because of non-performing loan difficulties. Singh suggests that more Indian commercial banks are now chasing project finance opportunities, and liquidity has improved, not deteriorated, as a result.

In the power sector, another banker says four IPP projects reached financial close in the first half of 2004, the 550MW coal-fired Raigarh project (costing IRP21.4 billion, the gas-fired 464MW, IRP14.5 billion Gautami power, the 1,015MW IRP42.98 billion Mangalore thermal power project, and the 100MW IRP548 billion Mallana II hydroelectric power project. These power projects were also funded by local banks and development institutions.

Foreign investor interest in the power market has at least been revived thanks to the new Electricity Act 2003. According to Abhay Rangnekar, ANZ's country manager in India, the act gives independent power producers scope to develop power plants without relying on the State Utility Boards for offtake. "Thanks to the act, companies that have their own distribution network will be able to build power generation facilities and sell direct to major corporates," he says.

In general, the international banking community is approaching the Indian market on an opportunistic basis, foreign banks, for instance, are bidding for the financing of the Jawaharlal Nehru Port Trust (JNPT) port project in Mumbai because of strong relationships with one of the sponsors, AP Moller. The financing is expected to be between $75 million and $100 million.

Rangnekar expects foreign lenders to be more visible in upstream oil and gas projects. "There aren't many projects involving the international oil majors, but mid-sized international sponsors, such as Cairn are currently active and will attract foreign lenders," says Rangnekar. ANZ is also eyeing natural resource developments, notably potential financings in the aluminium sector.

While the BIAL project and the planned privatisation and redevelopment of the Mumbai and New Delhi international airports have put the air transport sector in the project finance spotlight, Rangnekar suggests that there will only be a handful of other airports projects of sufficient scale to warrant a substantial project financing.

Another airport scheme, involving the construction of a new airport in Hyderabad, has stalled following the award of the concession to GMR Infrastructure (advised by ANZ). Rangnekar would not comment on the reasons for the lack of progress, but another financier indicates that negotiations faltered over the level of subsidy from the state government. The source says: "the bidder won on the basis of a certain level of state subsidy. The state government, however, has since indicated in isn't prepared to provide as much support in the early years as the private sector had previously assumed." It is not clear when the Hyderabad project will be resumed.